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October 15, 2003

EX PARTE

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements, WC Docket No. 02-112; 2000 Biennial Regulatory Review Separate Affiliate Requirements of Section 64.1903 of the Commission's Rules, CC Docket No. 00-175

Dear Ms. Dortch:

Yesterday, Clint Odom, Joe DiBella, Alexandra Lipecki, and Fred Moacdieh of Verizon met with Renee Roland Crittendon, Brent Olson, Pam Megna, Ben Childers, Bill Kehoe, Gail Cohen, Bill Dever, and Jon Minkoff to discuss matters associated with the above-referenced dockets. The attached handouts used in the meeting.

Should you have any questions, please feel free to call me directly.

Sincerely,

Clint E Odom

Attachment

cc: Renee Roland Crittendon

Imputation of Access Charges

- Section 272(e)(3) requires the BOC to "charge the affiliate described in subsection (a), or impute to itself (if using access for its provision of its own services) an amount for access to its telephone exchange service and exchange access that is no less than the amount charged to any unaffiliated interexchange carriers for such services."
- This is incorporated into biennial audit procedures in section 53.209(b)(3)(iii).
- After sunset, the accounting rules will continue to require imputation of access charges;
  - If long distance service is provided by the BOC directly rather than through a separate affiliate as a nonregulated service, it is subject to the Cost Allocation Manual and costs are assigned prior to separations. Section 64.901(b)(1) requires that "Tariffed services provided to a nonregulated activity will be charged to the nonregulated activity at tariffed rates."
  - If long distance service is provided by the BOC directly rather than through a separate affiliate as a regulated service, costs flow through to Part 69 and are allocated to the interexchange category, as they are to corridor services today (see, e.g., section 69.401). Price cap rules require the BOC to impute access service revenues for its interexchange services. See LEC Price Cap Order, 5 FCC Rcd 6786, para. 174 (1990); Application of Access Charges to the Origination and Termination of Interstate, IntraLATA Services and Corridor Services, 1985 FCC LEXIS 3510, FCC 85-172 (1985).
  - If long distance services continue to be provided through a separate affiliate, section 32.27(c) requires the BOC to record revenues for access services provided to the affiliate at tariffed rates.

Substitutability with Wireless

- LECs are losing roughly the same number of lines to wireless and cable as they are to CLECs
- At least 10 million lines have migrated from wireline to wireless
- For last three years, number of LEC lines have declined after a century of steady growth
- Number of wireless lines has increased from 69 million in 1998 to about 149 million today and are still growing. By next year, there could be more wireless subscribers than LEC wireline subscribers (currently about 162 million and declining)
- Rapidly growing number of customers use wireless as a substitute for second lines, and about 3 percent have abandoned wireline entirely
- Currently, wireless carrier revenues are more than half of wireline revenues
- Nearly half of wireless customers make the majority of their calls from wireless phones rather than wireline
- 16 percent of wireless subscribers use their service to replace wireline
- About 30 to 50 percent of 911 calls are wireless (Tom Sugrue)
- Universities have lost 40 percent of their telephone service revenues to wireless
- Per minute price for wireless has dropped below wireline (9-12 cents per minute compared to 10-15 cents for wireline)
- Wireless bundles and free weekend calling have contributed to wireline substitution
- Sources;
  - White paper
  - IDC study
  - Deutsche Bank
  - Kaufman Brothers

Substitutability with Other Platforms

- Cable Telephony
  - Cable broadband investment allows addition of telephony at low incremental cost
  - Cable offers telephony to 14 million households and has 3 million subscribers
- Voice over Internet Protocol
  - $2.2 billion in revenues in 2001
  - Increasing deployment of packet switches will drive voice growth
- E-mail, Instant Messaging
  - 92 percent of online users say e-mail replaces 39 percent of their long distance calls
  - 53 percent of broadband users have used Instant Messaging as a substitute for long distance calls
  - 31 million households used IM in 2002

Bundling

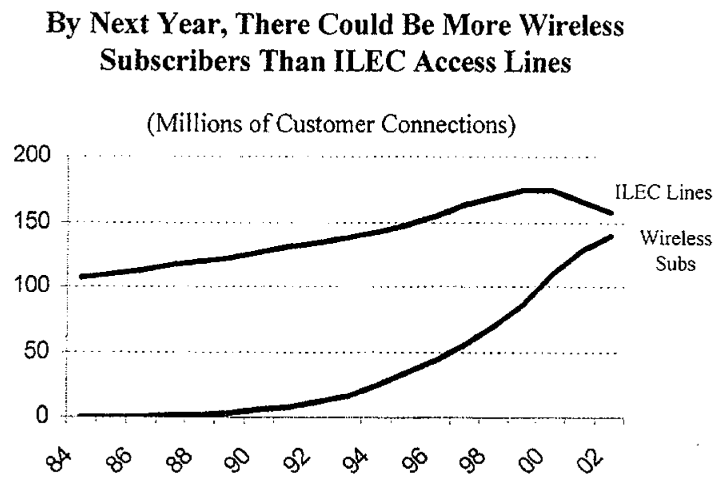
- Bundling defined as package of services priced below sum of individual components
  - May include local, long distance, broadband, wireless
  - May include "block" of long distance minutes or unlimited long distance calling
- Long distance carriers introduced bundles years ago, first with Enterprise market and later consumer wireless and wireline markets
  - AT&T Virtual Telecommunications Network Service for business in the 1980s
  - Later, AT&T (OneRate USA), MCI (Neighborhood Complete), Sprint (Complete Sense), Z-Tel (HomeLine), Excel (MyLine), VarTec (OneChoice), Talk America (Nationwide).
- Verizon has data on its customers using bundles v. unbundled long distance but not for other interexchange carriers other than published reports
  - Verizon Freedom includes unlimited long distance calling
  - Measured plan offers 5 cents per minute
  - Freedom All includes DSL plus wireless

Special Access Competition

- FCC found that the market was competitive and established collocation triggers for allowing pricing flexibility
- FCC recognized that rates might increase in pricing flexibility areas since regulatory controls may have caused special access to be priced below cost
- In response to pricing flexibility, Verizon has realigned its rates to reflect the market, where CLECs generally offer higher month-to-month rates and lower discounts and contract offerings
- Verizon's special access rates in price flex areas have increased in some instances and decreased in others
- Verizon has offered numerous contract price discounts in price flex areas that substantially reduced interexchange carrier costs
- Verizon's special access rates are 32 percent below the level prevailing in the early 1990s
- AT&T, MCI and Sprint have 90 percent of the Enterprise market
- CLECs have 36 percent of the special access market
- AT&T has built 18,000 miles of fiber in 90 cities and has 7,000 buildings on net
- AT&T gives more than half of its local dedicated access orders to CLECs rather than ILECs

Wireless Competition

- The Cellular Telecommunications & Industry Association reports nearly 150 million mobile wireless subscribers.[1] Considering the current growth rate of wireless subscribers, there will soon be more wireless subscribers than wired ILEC lines in the U.S.



Source: FCC competition reports and CTIA Semi-annual Wireless Industry Survey results

- Besides the convenience of mobile services and its features, wireless services have become very affordable. According to the Bureau of Labor Statistics, consumer prices for cellular phone service have fallen 30% and average revenue per minute has fallen 70% in the last five years.[2] These wireless services sometimes include free weekend calling, bucket pricing, free Caller-ID, free paging, free first minutes and so on. The larger wireless local calling areas can result in free intraLATA toll calls, as well as long distance calls, depending on the wireless plan.

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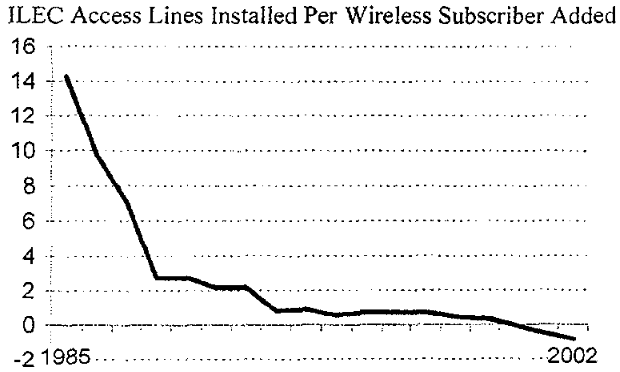
[1] The figure came from their homepage www.wow-com.com as of Aug. 4, 2003.

[2] Prices are from CPI-W, cellular telephone services data, detailed statistics downloaded from www.BLS.Gov; and average revenues per minute are from the Semi-Annual Wireless Industry Survey, CTIA, Washington, DC, Dec. 2002.

- Consumers have choice among wireless providers. Three or more mobile competitors cover ninety-five percent of the U.S. population, and six or more wireless competitors serve seventy-one percent of the population.[3] Therefore, including wireless providers as a competitive alternative to wired-based services means the inclusion of several meaningful competitors.

- The degree of wireless replacement of wireline services is appearing in the basic data, as well as research studies. As **Figure 10** shows (below), in 1985 there were fourteen ILEC access lines installed for every wireless subscriber added. Today, there is roughly one access line lost for every wireless subscriber added.

Figure 10: Today, There is Nearly One Line Lost For Every Wireless Subscriber Added



Source: CTIA Semi-Annual Wireless Industry Survey and Trends in Telephone Service, FCC, August 2003, Table 7.1.

- Not only are there millions more wireless subscribers added each year, but also these subscribers are using their wireless services to a much greater extent than before, thereby replacing wireline use. For example, the average wireless subscriber generated 229% more minutes-of-use in 2001 than the average wireless

[3] Eighth Annual CMRS Competition Report, FCC, FCC 03-150, WT Docket 02-379, Released July 14, 2003, Appendix D, p. D-9, Table 5.

subscriber in 1997, indicating that wireless consumers are calling more and talking longer than in previous years.

- Mounting empirical evidence supports this growing trend in wireless substitution.
    - In 1998, Southern Media & Opinion Research found that nearly half of wireless subscribers made the majority of their calls from their mobile telephone, rather than from their home telephone.
    - About one-quarter of African Americans have cell phones but a new Parks Associates report found that in the next 12 months, 31% of the remaining black population without cell phones plans to purchase one.
    - The following year, Peter D. Hart Research Associates reported that 38% of wireless customers had at least some interest in using wireless to replace their home telephone use.
    - The same year, M/A/R/C Research found that 16% of wireless subscribers used their service to replace wireline services.
    - Thomas J. Sugrue, the FCC's Wireless Bureau Chief estimates that 30% to 50% of emergency calls (i.e., 911 calls) are made from mobile phones, accounting for more than 50 million local calls made on wireless networks. He also cited wireless substitution for wireless services among the FCC staff.[4]
    - A number of universities that provide telephone services to students on campus have lost hundreds of thousands of dollars, as some students are disconnecting the university's wireline service for the wireless service of their choice[5] and, according to one report, the revenues of university supplied telephone services has fallen 40%.[6] "It's cheaper to use a cell phone," one student has claimed.[7]

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[4] Thomas J. Sugrue, Opening Remarks, Sixth Annual CMRS Competition Report, June 20, 2001. His presentation includes a chart entitled "Wireline Substitution in the Wiener-Goldstein Household" that shows how the Chief of the FCC's Auctions and Industry Analysis Division saved $8.45 per month by buying a wireless services, instead of adding another telephone line.
[5] Stefanie Frith, "Students' Cell Phones Cost Colleges," *Associated Press*, New York, June 24, 2002.
[6] "Colleges Get Wake-Up Call from Cell Users," San Diego Business Journal, Sept. 23, 2002.
[7] Ibid.

Substitutability Sources

Vik Grover & Richard Fetyko, *Initiation of Coverage: Verizon Communications, Inc.: A General Flavor of Mild Decay*, Kaufman Bros., L.P. (July 14, 2003)

Scott Ellison, *U.S. Wireless Displacement of Wireline Access Lines Forecast and Analysis, 2003-2007*, IDC (Aug. 2003; IDC # 29969)